

# International arbitration in 2021

Illuminating the top trends



Freshfields Bruckhaus Deringer

# Welcome to our annual international arbitration top trends publication for 2021.

2020 turned out to be a year no one expected. With the fallout from the pandemic expected to continue well into 2021, we can expect further turbulent times ahead. However, with the widespread roll-out of vaccine programmes, we hope that 2021 will see the beginning of a global economic recovery and a return to a 'new normal' as we start to look beyond the pandemic.

In this edition of our top trends report, we explore the key themes that we predict will be important for our clients and arbitration practitioners during the year ahead. The following trends have been identified by international arbitration specialists from across our global network.

- The extensive use of remote hearings during the pandemic has shown that in many cases they work as an efficient and cost-effective alternative to in-person hearings. Once in-person hearings become an option once again, we expect parties and tribunals to consider how and when virtual hearings should continue to be a feature of the arbitral process going forward.
- COVID-19-related disputes leading to arbitration have come in waves. Government assistance packages and temporary renegotiation of contracts have prevented an anticipated major spike in cases. However, contractual disputes have arisen on the scope of *force majeure* clauses, and some governments have used the pandemic as a pretext for political changes. Yet others have buried their heads in the sand and taken no relief action for certain sectors. This may give rise to claims for those investors who benefit from an investment treaty.
- Corporate insolvencies are expected to rise sharply in most major economies around the world. Where an arbitral counterparty is insolvent, or at risk of becoming insolvent, the case strategy needs to be carefully managed to minimise the risks associated with insolvency and the arbitral process.
- Investment protection in the EU and UK will be an area to watch in 2021 as the effects of the agreement terminating intra-EU bilateral investment treaties (BITs) and the UK's formal departure from the EU take hold. It is not yet clear what approach the UK will take in its future trade agreements, but the lack of investor-State dispute settlement provisions in the new EU-UK and Japan-UK trade agreements indicates that UK investors will increasingly need to rely on the UK's BIT network to protect their investments.
- Recent government policy reforms in the energy, technology and finance sectors, particularly in Latin America, may lead to new investment treaty claims being filed by affected investors in coming months, in addition to claims relating to government measures taken in response to the pandemic.
- Recent reforms of some of the major arbitral institutional rules have paved the way for the more efficient conduct of arbitrations, with increased tools, procedures and technology at the tribunal's and parties' disposal.
- The pandemic has hit the international construction and infrastructure industry hard. The combination of the market uncertainty, reduced finance available and a hardening of both national and commercial protectionism is likely to lead to more disputes as ongoing projects reach completion and the parties seek to address the economic realities of the pandemic.

- Given the recent focus on arbitrators' duties of disclosure following the UK Supreme Court Judgment in *Halliburton v Chubb*, we analyse the current state of play on the topic from an international perspective.
- With an increasing focus on sustainability globally, our final trend evaluates the role that arbitration plays in the context of resolving climate change disputes and looks at how the arbitration process itself can be more sustainable.

We look forward to navigating the challenges and opportunities presented by these developments with our clients during the year ahead. Through looking ahead, we can help to more effectively and strategically plan and prepare for what comes next.

Read on to explore these trends in more detail. If you would like to discuss any of the topics covered in the report, please reach out to us, the authors of the trends or your usual Freshfields contact.



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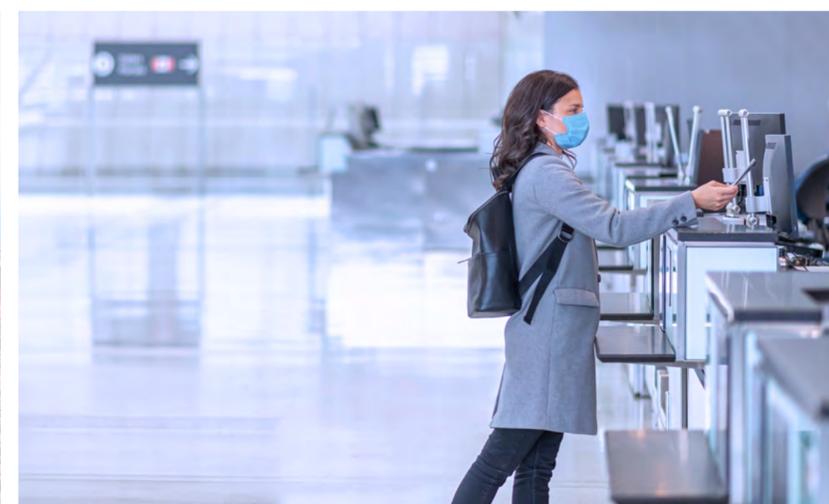
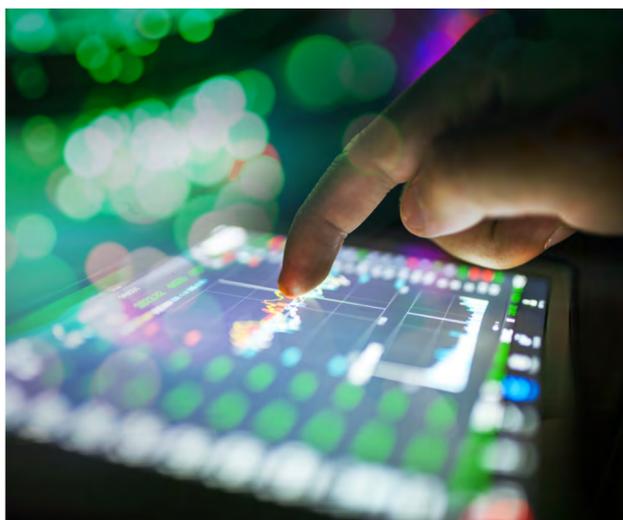
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# International arbitration in 2021



# 01

## The future of remote hearings in a post-pandemic world

The COVID-19 pandemic has had an unprecedented impact on the arbitral process.



# 01 The future of remote hearings in a post-pandemic world

The COVID-19 pandemic has had an unprecedented impact on the arbitral process. At the start of the pandemic, several hearings were postponed due to travel restrictions and social distancing measures. Nevertheless, illustrating the adaptability and flexibility of arbitration, several tribunals and arbitral institutions quickly adapted by ordering remote hearings. Indeed, since the start of the pandemic, relatively few hearings have been held entirely in person, with most being semi- or fully remote. According to a recent survey conducted by the ICC, by Q4 2020, 71 per cent of users had participated in fully virtual hearings, an increase from 36 per cent in Q1.

Given the absence of express provisions addressing remote hearings in most arbitral rules or national arbitration legislation at the start of the pandemic, many arbitral institutions promptly released guidance to assist arbitration users. Examples include *COVID-19: Information and Guidance in SCC Arbitrations* (27 March 2020); *ICC Guidance Note on Possible Measures Aimed at Mitigating the Effects of the COVID-19 Pandemic* (9 April 2020); and *HKIAC Guidelines for Virtual Hearings* (14 May 2020).

Non-institutional guidance was also released in the form of external protocols, notably the Seoul Protocol on Video Conferencing in International Arbitration, and Africa Arbitration Academy's Protocol on Virtual Hearings in Africa; and model procedural orders, such as the CPR's Model Procedural Order for Remote Video Arbitration Proceedings and PLC's Procedural Order for Video Conference Arbitration Hearings.

Many arbitral institutions have now taken steps to update their rules to provide expressly for the use of remote hearings. For example, Article 19.2 of the LCIA Arbitration Rules 2020 now provides that 'a hearing may take place in person, or virtually by conference call, videoconference or using other communications technology with participants in one or more geographical places (or in a combined form)'. Similarly, Article 26.1 of the new ICC Arbitration Rules 2021 provides that '[t]he arbitral tribunal may decide, after consulting the parties, and on the basis of the relevant facts and circumstances of the case, that any hearing will be conducted by physical attendance or remotely by videoconference...'.  
These changes will help to minimise the risk of due process challenges on the basis of a tribunal's decision to order a remote hearing. Indeed, in a recent decision of the Austrian Supreme Court in Case No. 18 ONc 3/20s, the Court confirmed the Tribunal's power to hold remote hearings over one party's objections and rejected due process concerns. We anticipate that this general approach will, by and large, be followed by courts in arbitration-friendly jurisdictions.

However, will a post-pandemic world be different? How should tribunals assess the pros and cons of a merits hearing where there are no impediments to travel? With this in mind, ICCA recently launched a research project entitled 'Does a Right to a Physical Hearing Exist in International Arbitration?'.  
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## ICC 2020 Industry Survey Results

Released in November 2020

### Q1 2020

36%

of users had participated in fully virtual hearings

### Q4 2020

71%

of users had participated in fully virtual hearings



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# 01 The future of remote hearings in a post-pandemic world

The reality is that remote hearings can work, and we have seen several successful examples of this. The technology used to facilitate remote hearings is now well established, with significant improvements made in terms of functionality to better suit the needs of remote hearings. Indeed, remote hearings have already become more sophisticated and physical hearing centres have started adapting their spaces to cater for a future with remote or partially remote hearings being the norm. There are also many advantages to remote hearings, including cost efficiency. Hearings are expensive and remote hearings have the obvious advantage of promoting savings on flights, accommodation and hearing centre costs.



**Fewer flights, and a shift from paper to online hearing bundles, also results in a significantly lower carbon footprint, which fits into the broader initiative, led by the likes of the Campaign for Greener Arbitration, of making arbitration more environmentally friendly.**

Stephanie Mbonu, Global IAG Project  
and Hearing Manager

Debates as to whether hearings should be remote, in person or a combination of the two will now be a regular feature of the arbitral process. Tribunals will need to take into account a number of factors when deciding whether to hold remote or in-person hearings, including: (i) the nature of the evidence and whether an in-person hearing would assist with the resolution of the dispute; (ii) the size and complexity of the dispute; (iii) technological considerations; (iv) time zone considerations; and (v) any justifiable concerns regarding witness tampering.

Against this background, remote hearings may well become the default position for smaller, less complex cases, as the efficiency gains far outweigh any due process risks. By contrast, for larger and factually complex disputes, we expect many tribunals to prefer the practice of in-person hearings, perhaps with certain remote components where appropriate.



**Provided that tribunals exercise their discretion in a thoughtful and reasoned manner, taking into consideration the views of both parties, the issues in dispute and under no circumstances putting personal preferences first, users of arbitration will benefit significantly from the availability of remote hearings in a post-pandemic world.**

Sami Tannous, Partner



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# 02

## COVID-19-related disputes: trends and predictions

How will COVID-19 shape the disputes  
landscape over the coming year?



## 02 COVID-19-related disputes: trends and predictions

### How will COVID-19 shape the disputes landscape over the coming year?

COVID-19 shaped and upended almost every facet of life across the globe in 2020, and arbitration is no exception. In addition to its pervasive impact on arbitration procedure (discussed in trend 1), COVID-19 has given rise to new disputes, many of which are being – or likely soon will be – resolved through arbitration. As with the pandemic itself, COVID-19-related arbitration disputes have come, and we expect will continue coming, in waves.

#### First wave: *force majeure*, frustration and MAC

Unsurprisingly, the first wave hit those industries that are most directly and severely impacted by COVID-19, including, for example, aviation, retail, real estate, oil and gas, and fintech. Many companies have found themselves unable to fulfil their contractual obligations due to government restrictions, including national lockdowns and closure of borders. While some have been able to renegotiate contracts or reach agreement on deferring performance and/or payment, many others have been unable to resolve amicably the disputes arising from the consequences of COVID-19.

The resulting disputes often revolve around questions of *force majeure*, frustration and material adverse change (MAC) provisions in contracts, or similar legal doctrines that may excuse performance.

### *Force majeure*



Some jurisdictions (such as China and Japan) recognise *force majeure* as part of their civil law, while others (such as England and Wales, and New York) require an express contractual provision. In either case, a party may be excused from performance of contractual obligations affected by causes outside the party's control, possibly including the pandemic.

### Frustration



Frustration can excuse obligations on the grounds of an unforeseen event that makes performance impossible (eg contracts for the supply of goods that can no longer be produced due to government measures shutting down plants). One issue expected to arise in this context is whether the second and third waves of COVID-19, and the attendant recurring lockdowns and restrictions, are sufficiently 'unforeseeable' to support a frustration claim.

### MAC



Commonly used in M&A, MAC clauses allocate to the seller the risk of something happening before closing that has, or at some time in the future may have, a materially adverse effect on the business. MAC clauses are often used as a basis for renegotiation – sellers are willing to renegotiate terms to avoid litigation uncertainty and the associated reputational damage of a claim.

### Supervening hardship/ change of circumstance



In some jurisdictions (typically civil law jurisdictions), a party may be able to terminate a contract where its performance becomes too burdensome as a consequence of the COVID-19 outbreak.

### Economic impossibility



Statutes also may provide for economic impossibility, incapacity or delay to allow withdrawing from or amending the contract, including postponing deadlines. Contracts also may contain express terms to this effect, as well as price review and change of law clauses.



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## 02 COVID-19-related disputes: trends and predictions

Courts and arbitral tribunals worldwide have grappled with COVID-19-related disputes involving the above clauses. While most arbitrations remain confidential, courts have delivered some important judgments that serve as useful precedent, including as persuasive jurisprudence for arbitral tribunals, in an area that is largely untested. For example, the English High Court has decided COVID-19-related cases claiming *force majeure* in the aviation sector (in which it found on facts that there was no *force majeure*) and MAC in the fintech sector (in which it laid down important standards for when a MAC occurs). Similarly, the Delaware courts saw a number of MAC disputes in the retail sector, including the dispute over LVMH's obligation to complete its acquisition of Tiffany's, and a number of other disputes are presently ongoing.

Interestingly, some States have officially declared COVID-19 to constitute a *force majeure* event, and China has issued *force majeure* certificates to companies that seek to excuse non-performance. Meanwhile, the UK government issued non-binding guidance on 'responsible contractual behaviour in the performance and enforcement of contracts impacted by the COVID-19 emergency' in May 2020, which may assist parties and adjudicators in determining what constitutes reasonable behaviour in the wake of COVID-19 disruptions. The weight given to such State guidance in a dispute remains to be seen.

### Subsequent waves: earn-out disputes and construction arbitration

In addition to disputes caused directly by COVID-19, further disputes are likely to arise from the economic turmoil accompanying the pandemic.

One example is disputes arising from 'earn-out' clauses, which provide that the seller of a business will receive future additional compensation if the business achieves certain agreed-upon financial goals. A common mechanism in many M&A transactions (particularly in the life sciences sector), earn-out clauses have a reputation for generating disputes, and arbitration has become a primary forum for the resolution of these disputes. COVID-19 disruptions have led to divergent views about the risks to a particular business, resulting in a surge in the use of earn-out provisions across a number of sectors as a way to move forward with a transaction in the face of such uncertainty. More earn-out clauses mean more opportunities for parties to disagree on whether they have been triggered. Thus, 2020's wave of COVID-19-induced earn-out agreements may turn into 2021's (or 2022's) wave of earn-out arbitrations.

Construction arbitration – particularly in the transportation, renewable energy and telecom sectors – is another space to watch for the consequences of COVID-19's disruptive force. As discussed further in trend 6, COVID-19 is expected to cause a myriad of problems for major construction projects, ranging from potential

insolvency of major contractors and crucial supply chain vendors, to ongoing travel restrictions that disrupt 'fly-in, fly-out' employment models for projects, to uncertainty and instability in the credit market, upon which large construction projects depend.

So far, the continuation of government protection programmes, the personal impact of the pandemic and the cost involved in bringing proceedings have all contributed to keeping the surge of disputes expected by some at bay. However, as the pandemic is brought under control, government protection schemes are lifted, and agreements to defer or reschedule performance or debt expire, we expect parties to look at their options closely and more disputes will crystallise.



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## 02 COVID-19-related disputes: trends and predictions

### Quantum issues across the waves are likely to raise further challenges

We also expect COVID-19 to lead to significant disputes around novel quantum issues. Parties may seek to rely on the impact of COVID-19 to either reduce or increase the damages they seek from contract breaches that happened just before COVID-19 (or in its early stage). Respondents may argue that the pandemic would have led in any event to the contract being rendered ineffective or less profitable; and claimants operating in sectors that benefited from COVID-19 may argue that they should be compensated for the massive additional profit they lost because of the breach. Valuations also will likely become more difficult, as questions of whether to take into account a company's COVID-19-caused loss, or how reliable historic cash flows are in a post-COVID-19 future, give rise to new complexities in the already difficult task of assessing damages in complicated cases.



**Parties, practitioners and tribunals will need to grapple with these issues on a case-by-case basis. Given that tribunals are afforded significant discretion when quantifying damages, there will almost certainly be a variety of different approaches adopted. This, in turn, is likely to lead to an increase in enforcement challenges and set-aside proceedings in national courts.**

Joaquin Terceño, Counsel

### Impact on investment arbitration

COVID-19 has also had an impact on investment arbitration. While government lockdown measures destined to control the spread of the pandemic that impacted business may (at least temporarily) be justified under doctrines such as state of necessity (or treaty exceptions such as public health measures), the failure to take measures compensating for the impact of such measures or the pandemic itself may breach positive obligations to grant fair and equitable treatment or full protection and security (or be potentially discriminatory if some sectors receive relief and some do not). We have also seen some governments invoke the pandemic as a pretext to reform certain sectors – for example, electricity in Mexico where alleged concerns over the reliability of privately owned renewable energy sources have led to measures prioritising the dispatch of thermal plants owned by the government's state-owned utility. Other governments have proposed or taken measures in the pensions sector in order to allow early withdrawal without considering the consequences such early withdrawal would have on the overall economics of protected pension fund administrators. The potential for COVID-19-related investment claims is discussed further in trend 6 below.

In short, the impact of COVID-19 on the arbitration landscape goes well beyond the growing comfort with virtual hearings and streamlined processes, as the pandemic's consequences can be expected to alter every stage of the dispute life cycle – giving rise to new claims, novel issues of liability and damages, and expanded opportunities to challenge the enforcement of awards.



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# 03

## Insolvency and arbitration

How to ensure that an award is worth more than the paper on which it is written.



## 03 Insolvency and arbitration

### How to ensure that an award is worth more than the paper on which it is written.

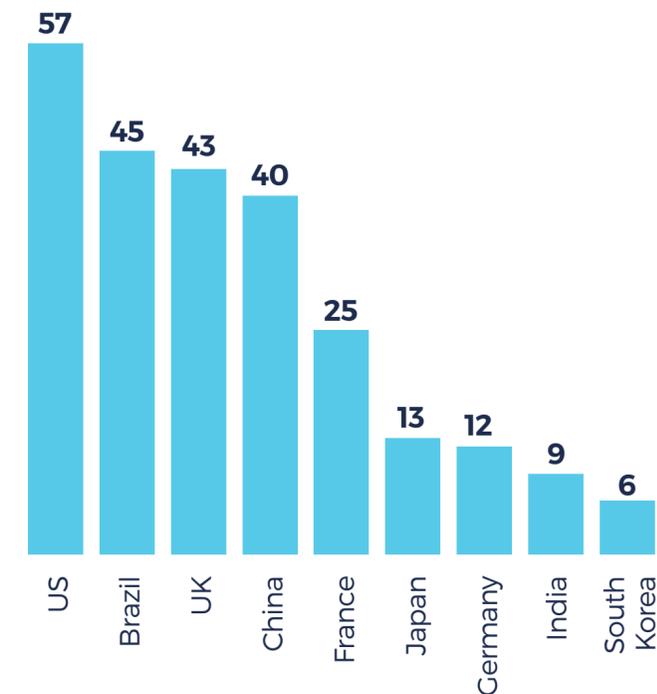
The pandemic has had a severe impact on a variety of industries, reducing air travel; shuttering hotels, restaurants and sports and other entertainment venues; and reducing sales for brick-and-mortar retailers and oil and gas companies, among others. Unsurprisingly, a number of countries have reported higher than usual insolvency statistics for the first half of 2020. At the beginning of the pandemic, certain governments put measures in place (including assistance packages) to pause or prevent insolvency filings. Coupled with the closure of courts, these measures probably prevented or delayed further corporate insolvencies.

According to various projections, the real effect of the pandemic on businesses will be felt in 2021, with corporate insolvencies rising sharply in most, if not all, major economies around the world, including the US, China, Japan, Germany, the UK, France and Brazil.

As insolvency becomes more prominent on the commercial landscape, it is important to consider the interplay between insolvency (or bankruptcy) regimes and arbitration. Critically, in certain jurisdictions a failure to adhere to local bankruptcy regulations can affect a party's ability to enforce an existing or future arbitral award or result in the setting aside of the award. When developing a case strategy, it is also essential to consider the interaction between the arbitral tribunal and the domestic courts, which monopolise the insolvency process, to ensure that the arbitration process goes smoothly.

### 2021 to set off avalanche of business insolvencies

Projected increase of business insolvencies in 2021 compared with 2019 (in per cent)



As of July 2020

Source: [www.statista.com/chart/22996/projected-increase-of-business-insolvencies-per-year/](https://www.statista.com/chart/22996/projected-increase-of-business-insolvencies-per-year/)



**The involvement of an insolvent party in an arbitration magnifies the potential impact of local courts in the arbitration and can create unexpected hurdles in enforcing the final award. To achieve the goals of the arbitration, the case strategy must be closely calibrated to these risks.**

Noah Rubins QC, Partner

### The effect of insolvency on arbitration

In most jurisdictions, the insolvency regime applies following a filing for insolvency (bankruptcy, administration or whatever the relevant local term might be) and a declaration by a domestic court. The court declaring a company insolvent will likely impose a number of conservatory measures to safeguard the company's assets that typically affect its creditors. It will also affect the company's legal rights and its existing and future legal relationships, including its handling of pending and future arbitrations.



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## 03 Insolvency and arbitration

A party's insolvency affects nearly all arbitral proceedings and each phase of an arbitration from the initiation of a dispute (including the validity of the arbitration agreement) through the pursuit of the arbitration to the eventual enforcement of an award. While States' insolvency laws vary – sometimes significantly so – there are some principles that are common to many jurisdictions. These principles include:

### Pre-arbitration



An arbitration agreement entered into prior to insolvency generally remains valid and binding on the insolvent party.

Companies in insolvency may conclude arbitration agreements, subject to the general restrictions on insolvent companies entering into contracts and the capacity of the insolvent companies to sign such agreements themselves.

### Pending arbitration



Certain jurisdictions require a (temporary) automatic stay of arbitration proceedings when insolvency proceedings commence (eg the US, England and Wales, and Hong Kong). In those circumstances, the court's permission is required to initiate or continue arbitration. That permission is typically granted with certain exceptions. In the US, for example, courts generally grant applications to lift the automatic stay unless the arbitration addresses issues that are 'core' to the insolvency proceeding, such as how a trustee of an insolvent party should distribute assets to creditors. On the other hand, in England and Wales the burden is on a creditor to make an application to the court to show that the leave would not impede the administration of the insolvent company.

The insolvency administrator often succeeds the insolvent party in the arbitral proceedings (replacing the insolvent party) and will continue with arbitration as the insolvent party would have done.

### Post-award proceedings



The insolvency of a party may potentially give rise to grounds for challenge of the award (eg in Germany, the award may be contrary to public policy – and thus can be set aside – when the arbitral proceedings were conducted with the wrong party, ie the original debtor instead of the insolvency administrator; or, in France or the US, an award may be set aside if the arbitral tribunal fails to stay the proceedings when the insolvency is opened).

Most insolvency laws prohibit enforcement of awards outside the insolvency proceedings.



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## 03 Insolvency and arbitration

Importantly, many insolvency laws have cross-border effects. In this regard, when considering or pursuing arbitration involving an insolvent company, a party should assess the potential requirements of the insolvency laws in question even if the insolvency and arbitration proceedings are seated in different jurisdictions. For instance, such is the situation in the US, England and Wales, and France. In particular, if the insolvency proceedings take place in the US, US courts may take the view that even arbitrations seated outside the US are subject to the US insolvency laws, which impose an automatic stay of any proceedings against an insolvent company, including arbitration, until allowed by the bankruptcy court to be resumed at the request of a party. Furthermore, US courts may determine that an arbitration award rendered outside the US without the authorisation of the US bankruptcy court is unenforceable in the US.



**Navigating an arbitration with an insolvent party requires a global perspective that accounts for the intricacies of each jurisdiction in which the debtor has assets. We work closely with the client and our colleagues around the globe to ensure that each step that the client takes maximises the likelihood for a fulsome recovery.**

Thomas Walsh, Special Counsel



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# 04

## Arbitration in the EU and UK: a changing landscape

Two major developments will affect the arbitration landscape in the EU and UK in 2021.



## 04 Arbitration in the EU and UK: a changing landscape

Two major developments will affect the arbitration landscape in the EU and UK in 2021: the UK's formal departure from the EU on 31 December 2020, and the agreement signed by 23 EU Member States terminating all intra-EU bilateral investment treaties (BITs) to which they are a party. In this trend, we explore what these developments mean in practice for the international arbitration community and our clients involved in arbitration in Europe.

### **Brexit – a new relationship for the EU and UK but no change to London-seated arbitrations**

On 31 December 2020, the transition period set out in the EU–UK Withdrawal Agreement came to an end, marking the start of a new chapter in the relationship between the EU and the UK. A last-minute trade deal was reached, the main aspects of which are embodied in the EU–UK Trade and Cooperation Agreement, which entered into force provisionally on 1 January 2021 (the Cooperation Agreement).

For those concerned about the recognition and enforcement of UK court judgments in EU Member States and vice versa, the Cooperation Agreement does not deal with this issue. The Recast Brussels Regulation ceased to apply to the UK at the end of the transition period, and the EU and UK have not negotiated any alternative regime to replace it. In April 2020, the UK formally requested accession to the Lugano Convention, which provides a framework for enforcing court judgments and to which the EU is a party (and Iceland, Norway and Switzerland), but the EU has not yet consented to the UK's accession and it remains uncertain whether the EU will do so.

Although the UK and Norway entered into a bilateral agreement to maintain reciprocal recognition and enforcement of court judgments after the UK's departure from the EU, for the time being at least, the only treaty framework for enforcing court judgments as between the rest of the EU and the UK is the 2005 Hague Choice of Court Agreements Convention (Hague Convention), to which the UK acceded in its own right on 1 January 2021. However, the Hague Convention is limited in scope to court proceedings brought pursuant to exclusive jurisdiction clauses, and to final judgments in such proceedings. Contracts with non-exclusive jurisdiction clauses or sole option clauses, and an order for interim relief are not protected under the Hague Convention. In these situations, parties will have to rely on any framework under local law in the country of enforcement, which may result in delay and additional hurdles or roadblocks in certain EU Member States.

In the meantime, parties who are concerned about the future framework for enforcing UK court judgments in the EU or vice versa may wish to consider opting for arbitration. The UK's departure from the EU will have no impact on the enforcement of arbitral awards: they will continue to be enforced in the same way under the New York Convention. In particular, as an alternative to litigating in the UK courts, parties may opt for arbitration seated in London. We expect that this will only enhance London's standing as one of the most popular seats for international arbitration.



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## 04 Arbitration in the EU and UK: a changing landscape

### Investment protection in the UK's new trading relationships

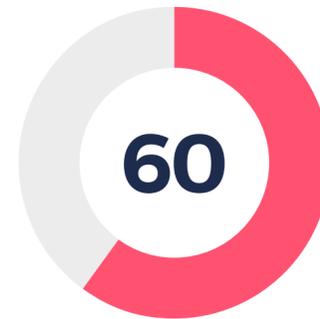
The UK's future trading relationship with the EU will be governed by the Cooperation Agreement. This has limited substantive investor protections and a higher threshold to qualify as a protected investor, and there is no investor-State dispute settlement (ISDS) mechanism for investors to rely on directly. The dispute settlement provisions are restricted to a WTO-style arbitration between the UK and the EU.

With respect to the UK's other trading arrangements, the UK is no longer party to the EU's free trade agreements (FTAs) and other international investment agreements (IIAs), such as CETA. The UK has made some progress in entering into new trade agreements to fill this gap, and we expect the UK to conclude more IIAs during 2021. Questions remain as to the extent of investor protection that will be available in such agreements. The new UK-Japan trade agreement, for example, like the EU-Japan agreement on which it was based, lacks any ISDS provision.

For all other countries without trade deals in place, trading will take place on WTO terms and the government has put in place a UK global tariff that will apply in such cases.

With respect to the UK's IIAs, investors will still be able to rely on the UK's extensive portfolio of BITs for protection. The UK's departure from the EU also means that there will be strong grounds for arguing that the UK's BITs with EU Member States should no longer be classified as intra-EU BITs for the purpose of the *Achmea* decision and the termination agreement recently signed by EU Member States discussed in detail below.

### UK trade agreements with non-EU countries



### new trade agreements took effect from 1 January to ensure continuity of trade with relevant countries

Trade agreements signed but not fully in effect with

Canada  
Jordan  
Mexico

Mutual recognition agreements have been signed with

Australia  
New Zealand  
US

Source: [www.gov.uk/guidance/uk-trade-agreements-with-non-eu-countries](https://www.gov.uk/guidance/uk-trade-agreements-with-non-eu-countries)



As the UK and the EU start a new chapter in their relationship, users of arbitration can be assured that the UK's departure from the EU will have no impact on the enforcement of arbitral awards as between the UK and EU Member States under the New York Convention. In addition, investors should continue to enjoy the protection of BITs between the UK and EU Member States, which are likely to remain in place after all intra-EU BITs are terminated in response to the ECJ's decision in *Achmea*.

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## 04 Arbitration in the EU and UK: a changing landscape

### Termination of intra-EU BITs

As predicted in past editions of our top trends publication, parties have continued to raise jurisdictional objections based on the 2018 *Achmea* decision, but without success. The European States' 2019 declaration in support of the *Achmea* decision has also received little support from arbitral tribunals, which have ruled overwhelmingly that they do not consider themselves to be bound by it.

Following the European States' 2019 declaration, 23 Member States signed an agreement terminating their intra-EU BITs (the Agreement) in May 2020. (Austria, Finland, Sweden, the UK and Ireland did not sign; Ireland did not need to sign, having already terminated its only intra-EU BIT.)

With immediate effect upon its entry into force (which takes place 30 days after ratification), the Agreement terminates 132 intra-EU BITs, including their sunset clauses, and 11 sunset clauses of intra-EU BITs that were terminated before the Agreement was signed. To date, the Agreement has entered into force for Bulgaria, Denmark, Croatia, Cyprus, Hungary, Malta and Slovakia. Spain also agreed to provisional application of the Agreement from 11 August 2020. There has been some academic discussion as to whether a State can terminate a sunset clause under a BIT. Investors may argue that such rights cannot be unilaterally revoked. The alternative view is that States have the power to vary and terminate treaties by mutual agreement in whatever way they wish, including sunset clauses. To date, this issue has not been tested in practice.

The Agreement also requires signatory States to inform tribunals in pending intra-EU arbitrations of the impact of *Achmea* on their jurisdiction, and to take steps to facilitate the termination of such arbitrations and related enforcement proceedings. Investors currently involved in pending intra-EU BIT disputes should therefore start planning their responses to such steps by respondent States. Although specific responses will have to be determined on a case-by-case basis, strategic considerations could include one or more of: (i) new proceedings under non-intra-EU BITs where available; (ii) commercial arbitration under an applicable contract; (iii) local court litigation; and/or (iv) negotiated settlements.

Notably, the Agreement does not cover intra-EU proceedings based on the Energy Charter Treaty (ECT), which are to be addressed at a later stage. This decision may be connected to the ongoing process to modernise the ECT, which the EU started in April 2020. However, Belgium is seeking an opinion from the European Court of Justice (ECJ) on whether the ISDS provisions in the draft modernised ECT are compliant with EU law. The question arises because the draft modernised ECT could be interpreted as permitting claims by an investor from one EU Member State against another EU Member State. The ECJ has not yet opined on the question of *Achmea's* application to the ECT, and to date arbitral tribunals have overwhelmingly accepted their jurisdiction in respect of ECT-based claims notwithstanding the *Achmea* decision.

# 23

EU Member States

signed an agreement terminating their intra-EU BITs in May 2020. This will terminate:

# 132

intra-EU BITs



**If the ECJ finds that the draft modernised ECT's investment protection provisions are incompatible with EU law for intra-EU disputes, investors may face additional legal hurdles in terms of jurisdiction and the enforcement of arbitral awards when bringing intra-EU claims under the current ECT. Therefore, investors seeking to safeguard their rights under international investment law will be trying to restructure their investments to secure the benefit of non-intra-EU BITs (eg through the UK), or conclude arbitration agreements directly with host States to secure their access to arbitration.**

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# 05

## The future of investor-State dispute settlement

Reform efforts continue amid  
ongoing legitimacy concerns.



## 05 The future of investor-State dispute settlement

### Reform efforts continue amid ongoing legitimacy concerns

In recent years, some States have challenged the use of arbitration in investor-State disputes. They have sought to reaffirm their rights as well as limit their obligations vis-à-vis foreign investors by renegotiating their international investment agreements (IIAs).

In Europe, the European Union (EU) continues to push for the establishment of a multilateral investment court (MIC) that would replace the arbitration system, notably in the current discussions on the reform of the Energy Charter Treaty.

However, unlike in other recent bilateral investment agreements with third countries (eg Canada, Vietnam), the EU has failed to secure investment court systems (pending the establishment of the MIC) in its latest international investments treaties with the UK and China (the latter of which only contains a commitment to pursue negotiations on this point within the next two years).

As discussed in trend 4, the UK is expected to clarify its stance on investor-State dispute settlement (ISDS) in the new IIAs it is likely to conclude in 2021 to fill the gap created by Brexit. In the meantime, questions remain as to the protection of investors in investor-State disputes post-Brexit, given the lack of such provisions in the EU-UK Trade and Cooperation Agreement and the Japan-UK agreement, which do not provide for any ISDS mechanisms.

More globally, some States have continued their efforts to strengthen their rights in IIAs in a shift away from traditional investor-State arbitration. Only two IIAs (Hungary-Kyrgyzstan and Japan-Morocco) out of the 17 concluded in 2020 will directly provide for arbitration in investor-State disputes, while others merely include commitments to further negotiate in this respect.

The US-Mexico-Canada Agreement (USMCA) – colloquially known as the ‘new NAFTA’ – entered into force on 1 July 2020. Pursuant to this trade agreement, the ISDS mechanism is only applicable to disputes between US investors in Mexico and Mexican investors in the US. Canadian investors in Mexico and the US (and vice versa) are no longer protected, with no ISDS between Canada and the US or between Canada and Mexico. Save in protected sectors (oil and gas, power generation, telecommunications, transportation and infrastructure), the substantive protections in the USMCA have been dramatically reduced in scope when compared with the NAFTA protections (no indirect expropriation or international minimum standard). Similarly, save in protected sectors, there are onerous preconditions prior to initiating arbitration (30 months before local courts).

Despite the criticisms and these restrictions on ISDS in new instruments, the 2020 Queen Mary Survey on ISDS highlighted that investors are generally satisfied with the current arbitration system for ISDS even while investors identify areas for improvement, including a proposed code of conduct of arbitrators and consideration of mandatory mediation. Notably, investors are generally opposed to the creation of a MIC (56 per cent).

### Investor satisfaction with ISDS

73%

satisfied with treaty-based arbitration

81%

for contract-based investor-State arbitration



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## 05 The future of investor-State dispute settlement

### Recent reactions to the legitimacy challenges

In response to the challenges levelled against ISDS, reform efforts undertaken at the institutional level are also progressing:

- Following its work on the improvement of ISDS, in November 2020 Working Group III of the United Nations Commission on International Trade Law (UNCITRAL) published for comment working papers on (i) an appellate mechanism (including the possibility to establish a permanent multilateral appellate body); and (ii) the selection and appointment of ISDS tribunal members (which refers to a Draft Code of Conduct for Adjudicators). The result of this consultation will be examined at the next session of Working Group III scheduled in February 2021.
- Working Group III and ICSID jointly developed the Draft Code of Conduct for Adjudicators. Apart from more traditional provisions on duties and responsibilities of adjudicators (including arbitrators) as well as disclosure obligations, the Draft Code also interestingly addresses ‘double-hatting’, ie adjudicators acting in different roles (counsel, arbitrator or expert) in several ISDS proceedings at the same time (by either enjoining adjudicators from double-hatting or, at least, disclosing it).

- The UNCITRAL Working Group II is also considering issues relating to expedited arbitration and the Secretariat is expected to prepare a revised draft of the expedited arbitration provisions in advance of Working Group II’s next meeting in March 2021.
- ICSID also continues its efforts to modernise its rules in order to increase transparency and efficiency in ISDS. In February 2020, ICSID published its Working Paper 4 setting out proposals for amendment of the ICSID rules, which focus, among other things, on disclosure of third-party funding.



**The different initiatives undertaken by various stakeholders to address the perceived shortcomings of ISDS will continue in 2021 and could be crucial as ISDS proves more relevant than ever for investors subject to a heightened risk of arbitrary State measures.**

Nathalie Colin, Partner

Another tool that is gaining traction in this context is mediation. With the 2019 United Nations Convention on International Settlement Agreements (the Singapore Convention) creating an internationally enforceable framework for settlements reached by mediation, and ICSID launching new draft Mediation Rules, the groundwork has been laid for investor-State mediation to play a more significant role. The newest generation of IIAs has started to include express provision for mediation or conciliation, albeit largely on a voluntary basis. We expect to see more debate on whether mediation has a greater role to play in ISDS provisions in treaties in the year ahead.



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## 05 The future of investor-State dispute settlement



**Just as the Singapore Convention generated a wave of interest in mediation of commercial disputes, it is similarly contributing to renewed interest in alternative and creative methods for the resolution of investor-State disputes, whether through mediation, conciliation or other forms of engagement short of full-scale arbitration. It may be that more States seek to include mandatory pre-arbitration conciliation or mediation requirements in treaties – so far, though, that remains extremely rare.**

Nicholas Lingard, Partner

### COVID-19's influence

As discussed in trend 6, measures and (announced) recovery plans adopted by States in response to the economic crisis may increase the risk of investor-State disputes in 2021. At the same time, if – and this remains the subject of heated debate – there is an avalanche of COVID-19-related claims, that is likely to exacerbate the existing legitimacy challenges to investment arbitration by stakeholders and the general public. Given the great impact of the pandemic on people's daily lives and the sensitive nature of the measures, challenges by private investors could put ISDS back at the forefront of the public debate. In this respect, the Columbia Center on Sustainable Investment has notably called for an immediate moratorium on all arbitration claims by private investors against States and for a permanent restriction on all arbitration claims in sectors affected by the COVID-19 pandemic.



**The COVID-19 pandemic has exacerbated the existing tensions recently focused on rejecting traditional international arbitration and rebalancing States' rights and obligations. Moving forward, investment structuring is bound to become even more crucial for investors who should seek to ensure that they benefit from effective ISDS protections.**

Lee Rovinescu, Partner



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# 06

## Investment arbitration trends

Which sectors and events do we expect to give rise to new claims in 2021?



## 06 Investment arbitration trends

### Which sectors and events do we expect to give rise to new claims in 2021?

The COVID-19 pandemic has led to unprecedented government intervention over the last year. Although there have been limited challenges against States under bilateral or multilateral investment treaties to date, we expect that further claims are likely to emerge over the coming year. Other contexts in which claims could arise this year include recent energy sector reforms, but also measures concerning less traditional forms of investments, such as those regarding new technologies and the banking and finance sector, particularly in the pension fund business.

### Government measures related to the COVID-19 pandemic

In order to cope with the effects of the pandemic, governments around the world have taken a wide range of measures that have affected all sectors of the economy. Foreign investors and their investments have not remained immune. In some instances, well-intended government measures have disproportionately affected foreign investments.

For example, as we discuss below, numerous countries have reformed, or are considering reforming, their pension fund regulations to allow participants to make early withdrawals, which will have a significant impact on the financial health of the funds, most of which are owned by foreign financial institutions.

A question in most COVID-19-related investment claims is likely to be whether governments, in parallel to the restrictions allegedly necessary to combat the spread of the pandemic, should have also adopted reasonable mitigatory measures or even rescue plans to ease or share the harm suffered by investors. Another question will be whether governments have used the pandemic as an excuse to further their political agendas unrelated to the health crises, at the expense of investors' acquired rights. Alleging that renewable energy generation poses a safety risk to the national grid in a context of reduced electricity demand owing to the pandemic, the Mexican government has taken measures to delay or prevent renewable energy projects from coming online, deliberately benefiting State-owned energy companies.

The crisis is far from over, and how deep the economic impact will be is still unclear.

### Pension funds

Investment arbitration is becoming increasingly popular among banks and financial institutions. In the last few years, claims have been filed in relation to the forced conversion of the currency of loans, as well as State bailouts and compulsory administration of banks in the midst of the financial crisis.

To add to these, in the next few months investment treaty claims may also arise from regulatory changes in the pension fund sector, particularly in Latin America. Arbitration proceedings have already been commenced by fund managers, so-called pension fund administrators or AFPs, against Argentina and Bolivia, due to the migration of the pension system back to public administration. In Chile, a similar initiative will be the object of a constitutional amendment to be debated in the course of this year. The role and remuneration of private pension funds is also under review in Mexico, Uruguay, Peru and Colombia. These proposals may gain support as States seek to tap resources from the pension system to finance COVID-19 recovery policies. The COVID-19 crisis has also led States to allow contributors to withdraw extraordinarily a certain amount of funds from their pension schemes, thus causing fund managers to incur unexpected operational costs to satisfy demands.



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## 06 Investment arbitration trends

### Energy

Recent times have witnessed policy reforms and legal changes in the energy sector in several countries. Modifications often amount to a retreat from previous programmes to incentivise private investment and increase energy efficiency, reduce carbon footprints and meet emissions targets. Through administrative, legislative and even court actions, programmes that typically included privatisations, promises of long-term legal stability and financial incentives, such as 'feed-in' electricity tariffs, are being abandoned or profoundly altered.

- In Mexico, for example, legislative changes in the electricity framework range from cuts in the income incentives for renewable energy projects, to the suspension of operation tests for new plants and to the alteration of dispatch rules, all apparently designed to favour the State-owned electricity company. In Peru, a supreme court decision has prompted proposals for a potentially adverse reform of dispatch rules for thermoelectric generators.
- In Chile, the government is planning to phase out completely all coal-based power plants by 2025.

- In Argentina, after years of tariff freezes in the gas and electricity sectors, the government has now forced a new renegotiation of remuneration regimes.
- The Ukraine government has significantly reduced the feed-in tariffs it had originally offered investors in the renewable energy sector. A similar measure was adopted by the French parliament at the end of last year.



**Measures such as these may give rise to a wave of international claims by foreign investors pursuant to investment protection treaties. It would not be the first time that sudden regulatory changes end up like this. The claims sparked by the Argentine emergency measures in 2002, and the more recent renewable energy cases against Spain, Italy and the Czech Republic, are the prime examples of what may come.**

Lluís Paradell, Counsel

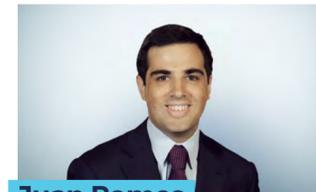


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## 06 Investment arbitration trends

### Technology

2020 has underscored the importance of the technology sector. It has proven crucial in remote working and in keeping the global economy going during the COVID-19 pandemic. With this increased focus on technology, investment in this sector is also likely to be greater than ever. At the same time, there are indications of mounting government intervention for security, tax and consumer protection reasons, given the absence, in many jurisdictions, of specific regulatory frameworks for new technology. For example, in Asia, China's new Export Control Law, which came into effect in December 2020, imposes certain export restrictions on sensitive technologies. A number of countries in Europe, including the UK, France, Spain and Italy, are seeking to collect a digital services tax from technology companies. In Australia, the government has been investigating competition and consumer protection issues in relation to digital platforms, such as Facebook and Google, which is likely to result in a regulatory intervention.

With more government involvement, the technology sector is likely to become more sensitive to State action and inaction, which, in turn, is bound to give rise to investor-State disputes. So far, technology companies have not resorted to investment arbitration in resolving such disputes as frequently as companies in other sectors. However, such arbitrations are on the rise. Reportedly, the Canadian taxi tech company Espiritu Santo has commenced arbitration proceedings against Mexico; and Uber has put Colombia on notice of a possible arbitration, following the government's ban of the use of the car-sharing app.

ICSID's case statistics demonstrate a rise in investment arbitrations in the technology sector from 2019 to 2020. This trend is likely to continue in 2021.

### ICSID's new cases in the information and communication sector doubled



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# 07

## Investment claims: project finance lenders have rights too

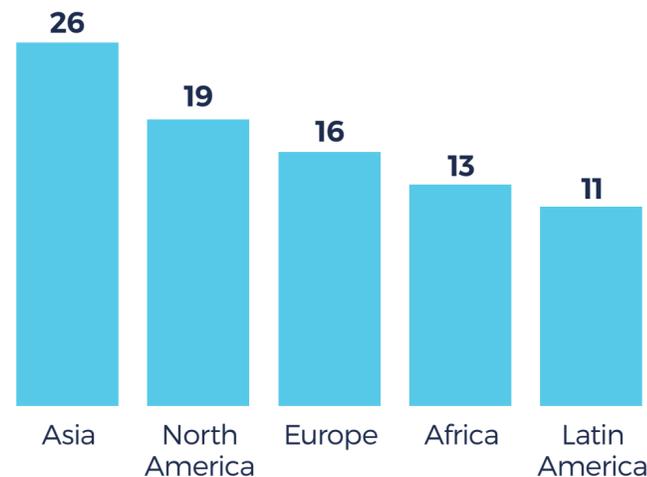
A recent award has opened the door for project finance lenders to seek compensation under international investment treaties.

## 07 Investment claims: project finance lenders have rights too

### A recent award has opened the door for project finance lenders to seek compensation under international investment treaties.

Project finance is critical to the construction of many energy, infrastructure, transport and industrial projects. In the energy sector alone, project finance transactions closed in 2019 globally amounted to \$85bn.

### Value of project finance transactions closed in 2019 by region (\$bn)



Source: IEA, Project finance transactions for power, by year of financial close in selected regions, 2015–2020

In addition to their economic importance, the commercial and investment risks borne by project finance lenders are significant. Among those risks is the possibility that governmental actions detrimentally affect a project's cash flows and, as a result, its ability to repay the project financing. Equity investors in projects often benefit from investment treaties that grant them protections against certain adverse State measures, including the right to seek compensation for damages arising from such actions through international arbitration. In contrast, it was unclear whether project finance lenders had access to such protections, despite the scale of their investments and of the risks they bore. That is, until the recent decision by the arbitral tribunal in *Portigon AG v Spain*.

### *Portigon AG v Spain* extends treaty protections to project finance lenders

In *Portigon*, the claimant had provided project financing to various renewable energy projects in Spain, which were detrimentally impacted by Spain's repeal of previously established incentives and a remuneration framework for such projects. The tribunal's jurisdictional decision, dated 20 August 2020, for the first time upheld the authority of arbitrators under an investment treaty (in this case, the Energy Charter Treaty) to decide claims by a project finance lender with respect to measures that were not directed against the financing itself, but rather against the financed project. This decision effectively extends investment treaty protections to project financing and project finance lenders.



**We expect an increasing number of project financiers to use investment treaty arbitration or at least the threat of arbitration to oppose unlawful State measures directed against financed projects and, if necessary, seek damages arising from such measures.**

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## 07 Investment claims: project finance lenders have rights too

### What protections are available to lenders?

International investment treaties stipulate specific protection standards for the benefit of foreign investors, including, among other things, protections against inequitable, arbitrary or discriminatory treatment, and expropriation without prompt and adequate compensation. Critically, investment treaties typically also provide investors with recourse to international arbitration directly against the government of sovereign States.

States may impair foreign investments in a variety of ways, including through legislative, administrative or even judicial acts. In the context of project finance investments, adverse State measures can take many forms, including:

- the repeal of a previously established remuneration regime including incentives and benefits for such projects (either by law or contract);
- breaches of contractual agreements entered into with State-owned entities; or
- the unilateral modification, termination or denial of concessions, permits or licences.

When State actions like these breach applicable investment treaties, the State must compensate the investor. For project finance lenders, potential damages might include losses suffered on long-term loan agreements, as well as other financial instruments (such as interest rate swaps) related to the project financing in question.

### What do lenders need to do to be protected?

To ensure that recourse to investment treaty protections is available when needed, it is vital that lenders keep an eye on several issues:

- **evaluate the structures of their transactions** to ensure the availability of optimal investment treaty protections. Investment treaty protection depends on the nationality of the party claiming protection (in this case, the lender). Providing the financing through the parent company or its branches or subsidiaries incorporated in different jurisdictions may have a significant impact on the investment protection available. A preliminary legal due diligence on the array of treaties available is therefore advisable;
- **maintain detailed records of their reliance on the host State's commitments.** As a third party to the relationship between the State and the project sponsors, it is important for lenders to keep a detailed record of any documentary evidence showing their reliance on certain State commitments (eg due diligence reports on statutory tariffs, governmental permits as conditions precedent, where available). Any direct interaction between the State and the lender will foster the lender's claim even where formal direct agreements with governmental agencies may not be available; and
- **draft with utmost care transfer, assignment and syndication agreements** to preserve treaty protection when syndicating, assigning or transferring the financing to third parties and clarify the entity (or entities) that can avail themselves of it.



**Project finance lenders have an opportunity to protect themselves against the risk of future adverse State measures that impair the economic viability of projects that they have financed. We are particularly well placed to advise lenders on their risk and investment strategy to secure the benefit of any available investment treaties.**

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# 08

## Latest arbitral rules reforms

Facilitating shorter, cheaper  
virtual arbitrations.



## 08 Latest arbitral rules reforms

### Facilitating shorter, cheaper virtual arbitrations

Driven by COVID-19 restrictions and user demands, arbitral institutions are arming tribunals with improved case management tools to deliver faster decisions, conduct remote proceedings and lower the cost of international arbitrations.

The COVID-19 pandemic has ushered in a new era of remote work and international arbitration is no stranger to this new reality. Contactless proceedings, whether fully virtual or under a hybrid model, are here to stay and will continue to be a feature of international arbitration practice in 2021, buoyed by advances in virtual hearing and electronic document management technologies. Responding to the global challenges posed by lockdowns, as well as to calls for greater expediency, transparency and cost-efficiency, leading arbitral institutions such as the ICC and LCIA have been taking steps to streamline their arbitration procedures. And other institutions such as ICSID, SIAC and DIAC are also in the process of revamping their rules to meet the demands of the moment.

The recently adopted ICC and LCIA Rules, as well as the ongoing ICSID amendment process, shed light on four key global themes that will set the tone for further institutional reforms in 2021 and beyond.

- **Summary dismissal, fast-track arbitrations and stricter time limits to issue awards.** Most arbitral institutions already allowed for some form of expedited and reduced-cost arbitral proceedings. Some of the more

recent reforms aim to expand access to such proceedings and impose stricter deadlines for tribunals to issue awards. For example, the new ICC Rules, which became effective in January 2021, have expanded the scope of application of such proceedings by increasing the threshold to opt out of expedited arbitration from \$2m to \$3m (amount in dispute). And under the latest iteration of the proposed ICSID Rules (Working Paper No. 4), parties will be able to opt in to expedited arbitration. In turn, the LCIA Rules, which came into force in October 2020, expressly recognise tribunals' authority to issue an order or award summarily dismissing claims that are manifestly without merit. And in a bid to reduce the average time it takes tribunals to issue their awards, the draft ICSID Rules currently establish an eight-month time limit from the last written or oral argument. Unlike the current ICC guidelines, however, which empower the ICC Court to reduce arbitrators' fees if they are unjustifiably late, the ICSID stipulation is a 'best efforts' one and does not set forth any penalties should a tribunal fail to issue its award within the prescribed eight months.

- **E-friendly and remote arbitrations.** In the COVID-19 era, some of the most notable innovations are designed to allow ongoing and new arbitrations to be held virtually. The recent LCIA and ICC reforms have refined and expanded their provisions on virtual or hybrid (semi-virtual) hearings, removing any ambiguities as to their feasibility or legality, and in some cases even empowering tribunals to order them regardless

of a party's opposition. Notably, these institutions have now embraced electronic communications and filings as the default rule, eliminating the need to submit hard copies, a welcome development that will help save costs and reduce the carbon footprint of arbitration proceedings.

- **More room for joinder and consolidation of proceedings.** In tandem with other reforms to promote efficiency, both the LCIA and the ICC have made it significantly easier to conduct multi-party arbitrations by broadening their rules on joinder and consolidation. The 2021 ICC Rules go as far as to allow the consolidation of proceedings involving claims between the same parties but under different arbitration agreements.
- **Increased transparency.** Heeding the call for greater transparency in both commercial and investment arbitrations, the new ICC and ICSID Rules require parties to disclose the existence (albeit not the terms) of any third-party funding agreement to avoid conflicts of interest between funders and arbitrators. Along the same lines, the ICC Rules allow for greater scrutiny of any changes of counsel throughout the duration of the proceedings and empower the tribunal to exclude newly appointed party representatives should their involvement create a conflict of interest. The LCIA Rules, in turn, now expressly regulate the role of tribunal secretaries.



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# 08 Latest arbitral rules reforms



We expect that these amendments will boost the continued and significant growth in the number of disputes resolved by international arbitration, and in the use of fast-track arbitration. Parties have more options to resolve their disputes in a faster and more cost-effective way and tribunals are empowered with a greater range of tools to ensure the arbitral process moves swiftly and efficiently, even in the face of an obstructive party.

Patrick Schroeder, Partner

The popularity of international arbitration appears to be growing. Evidence suggests that 2020 was a record-setting year for many arbitral institutions which saw their caseloads spike. The number of expedited proceedings and emergency arbitrations is also on the rise. The ICC recorded a total of 946 new cases in 2020 – the highest number registered since 2016 – while the LCIA and ICSID reported their highest ever number of cases.

The recent changes to arbitration procedure are aimed at promoting the efficient conduct of arbitrations. Over the last few years, the procedural toolbox available to arbitral tribunals has been expanded with a view to balance procedural efficiency with fundamental procedural principles, most importantly the right to be heard and the equal treatment of all parties. At the same time,

## 2019/2020 caseloads of the main arbitral institutions

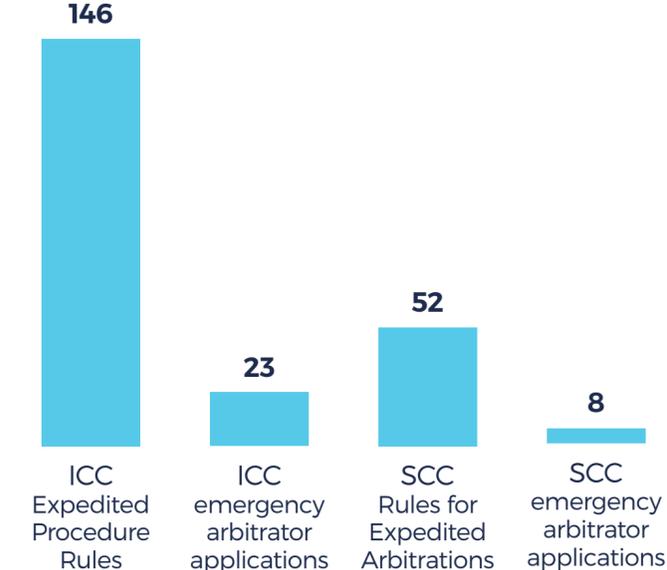
(total number of new cases, \*denotes a record number)



the COVID-19 crisis has reshaped the way parties, arbitrators and counsel go about dispute resolution. Arbitration as a flexible mechanism of dispute resolution is well placed to address the changing needs of stakeholders in that process.

## 2019 ICC and SCC statistics for expedited proceedings and emergency arbitrations

(total number of new proceedings)



The primacy of electronic communication and the option for remote hearings, which have gained popularity during the pandemic, are expected to stay and to lead to a more sustainable international arbitration process for years to come.



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# 09

## Continuing economic woes for the construction and infrastructure sectors

Is international arbitration in these sectors on the rise?



## 09 Continuing economic woes for the construction and infrastructure sectors

### Is international arbitration in these sectors on the rise?

The COVID-19 pandemic hit the construction and infrastructure sectors at a time when, in several markets, they were already economically strained. While many projects progressed successfully over 2020 (no doubt due to the commendable collaborative efforts adopted and the willingness of parties to negotiate and compromise), the effects of the ongoing pandemic will further challenge these sectors into 2021. Reduced consumer demand, lower revenue and an uncertain long-term outlook mean that the financial forecasts on which many projects were based now look optimistic at best. That is coupled with the additional difficulties – and hence cost – associated with execution of projects brought about by legislative changes (eg borders being closed), health implications (eg staff contracting COVID-19) and social distancing expectations (which materially impacts logistics). As we continue to see the longer-term economic realities of the COVID-19 pandemic crystallise in 2021, the true extent of the economic woes facing these sectors is starting to be understood.

We consider here three key issues that we predict will shape the international arbitration landscape in these sectors over the coming year.

### Less finance available for international projects

Reduced market liquidity coupled with suppression in investor risk appetite means there will be less finance available. We expect this will affect investors across the spectrum, from private equity to institutional investors as well as major asset owners and operators. This will make it increasingly difficult for many much-needed infrastructure projects to proceed. We expect that many previously approved projects will stall, leading to the instigation of arbitration by those reliant on the financial closing of those projects.

### The G20's Global Infrastructure Hub estimates that the world faces a

# \$15tn

infra spending gap over the next 20 years in both emerging and mature economies.

Source: <https://outlook.gihub.org/>

Moreover, while many States have announced plans to increase investment in infrastructure to drive forward economic recovery, these efforts may focus on domestic investments, with emerging economies losing out on

critical foreign investment. For example, even prior to the pandemic, China had cut its overseas lending through its Belt and Road Initiative by almost 95 per cent, from \$75bn in 2016 to \$4bn in 2019. At the same time, it has announced a new 'dual-circulation' economic strategy that prioritises domestic demand and technological innovation over closer integration with the outside world. This trend will continue into 2021 and, depending on how such policies are implemented, could cause an increase in arbitration if it leads to a renegeing on commitments or nationalisation of sectors and critical assets.



Perhaps a silver lining is the acceleration in the change of both public and corporate opinion towards sustainable and lower-carbon infrastructure, transport and energy. Many States have announced that low-carbon investment will be at the core of economic stimulus packages, creating opportunities for both investors and the market more broadly.

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## 09 Continuing economic woes for the construction and infrastructure sectors

### Financial distress of big market players

2020 saw ongoing financial distress throughout the construction and infrastructure sectors, with associated supply chains being particularly affected as cash reserves were depleted and future projects put in doubt. There are reports that in December 2020 alone 20 construction entities in the UK collapsed.

Moreover, last year saw a marked change in the willingness of States to prop up long-established and State-owned/backed companies. Major contractors (such as Arabtec in the UAE) have been casualties of the global downturn. Chinese State-owned enterprises have defaulted on their bonds, resulting in local government finance vehicles (collectively, the State's biggest spender on construction projects) struggling to raise capital and causing some to question the long-held assumption that the Chinese authorities would always bail out State-owned enterprises.

Looking forward over 2021, we anticipate an increased number of arbitrations in these sectors as cash-poor project participants struggle to meet their payment obligations on time and the acceptance of future payment promises becomes untenable.

### Increased focus on project securities

Given prevalent financial distress in these sectors that strains long-established relationships and erodes trust, we are seeing an increasing number of calls on project

securities, such as performance or retention bonds and parent company guarantees (both up and down the supply chain). We anticipate this will continue into 2021. That will lead to an increase in contractors commencing emergency arbitration to prevent the enforcement of project securities or, where this procedure is not available, court action for interim relief prior to the constitution of the tribunal (eg as occurred in the Sharjah Federal Court of Appeal Case No. 1015/2020 in the UAE). In addition, we expect issuers to apply greater scrutiny in response to calls on performance securities, which may, in turn, lead to formal dispute proceedings (eg the 2020 Hong Kong case of *West Kowloon Cultural District Authority v AIG* where the issuer refused to pay out on an on-demand bond). Consequently, instruments that were once considered 'as good as cash' are, in some jurisdictions, no longer as secure.

### Practical tips

As economic woes continue to bite, we set out below some practical actions that project participants can take to protect their position and attempt to resolve disputes quickly and amicably:

- ensure that contract governance/stewardship is properly followed and documented, including following the change of control procedures, and that calls on project securities are followed to the letter;
- undertake regular due diligence to understand the pressures and financial standing of counterparties;

- seek an early merits assessment of claims to allow for clarity on the strength of claims and to encourage commercial reality in setting strategy and understanding likely accounting on projects;
- consider third-party funding to pursue legitimate claims in arbitration to reduce the strain on resources and balance sheets; and
- consider making full use of alternative dispute resolution mechanisms, whether provided under the contract or otherwise, to narrow issues in dispute before commencing arbitration.



**These trends have been identified by global projects disputes specialists from across our network, who have been advising on these issues and closely monitoring trends in these sectors for decades.**

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# 10

## Arbitrators' duties of disclosure in the spotlight

In 2020, we saw several cases in different jurisdictions addressing arbitrators' duties to disclose potential conflicts.

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In 2020, we saw several cases in different jurisdictions addressing arbitrators' duties to disclose potential conflicts. An increasingly pro-transparency approach seems to be emerging internationally; arbitrators are being held to high standards, which is likely to inform what is considered international best practice. We expect this trend to continue in 2021 and beyond, as national courts and annulment committees continue to refine the legal position on these issues and apply them to different fact patterns and contexts.

Three cases in 2020 illustrate this trend.

- In June, an ICSID ad hoc committee in the *Eiser v Spain* case annulled a €128m award made against Spain under the Energy Charter Treaty following the claimant's nominated arbitrator failing to disclose his professional relationship (gained through his role as arbitrator and counsel in other arbitrations) with the claimant's damages expert.
- In November, the UK Supreme Court handed down its judgment in the case of *Halliburton v Chubb* (in which Freshfields represented the LCIA as an intervener in the Supreme Court appeal). The case concerned a challenge to remove the chair of a Bermuda Form ad hoc arbitration tribunal on the basis of apparent bias following his failure to disclose his subsequent appointment to the tribunal by one of the parties in a separate arbitration commenced by a third party. That subsequent arbitration arose out of the same 2010

Deepwater Horizon incident in the Gulf of Mexico and concerned similar issues. Although the Supreme Court dismissed the appeal and declined to remove the arbitrator, it provided welcome confirmation as to the test for apparent bias in the context of international arbitration and held that there is a legal duty to disclose facts that might give rise to the appearance of bias.

- In September, the Sao Paulo Court of Appeals annulled a commercial arbitration award following a presiding arbitrator's failure to disclose his subsequent appointment by one of the parties in an unrelated arbitration.

There were also a number of high-profile cases globally in which arbitrator challenges were dismissed and no breach of their duties found, but which nonetheless helped to clarify the expected scope of an arbitrator's duties.

- Germany failed in its second attempt to disqualify an ICSID tribunal from hearing a €4.7bn nuclear-related claim brought by Swedish company Vattenfall after alleging that an arbitrator had failed to disclose an issue conflict.
- In *Petroceltic v Egypt*, a UK oil and gas company failed to dislodge a French arbitrator from an ICSID tribunal on the basis of her repeat appointments by States including Egypt.
- In *Hope Services v Cameroon*, a different French arbitrator continued to hear the ICSID case against Cameroon

after surviving a challenge brought on the basis of his failure to disclose advocacy work performed for the State more than 30 years ago.

The precise test applied in each of these cases varied (eg with the Sao Paulo court applying a subjective test as to whether the non-common party's 'trust had been breached'; the ICSID committees considering whether there had been a 'serious departure from a fundamental rule of procedure'; and the UK Supreme Court considering how the objective 'fair-minded and informed observer' would assess the facts). But there was a common thread to all these cases.

Following these cases, in 2021 we expect to see heightened vigilance in relation to disclosure – both when the tribunal is being constituted and on a continuing basis. Arbitrators, parties and counsel will be expected to heed the warnings from these decisions and take all possible steps to avoid being caught up in similar challenges.

There remain some open questions as to the extent to which an arbitrator (or parties and counsel) is required to conduct due diligence to find out disclosable facts, and as to what facts should be considered disclosable at all. There also remain some uncertainties as to how arbitrators should navigate their competing duties of disclosure, confidentiality and privacy – though the *Halliburton* decision provides some guidance on this for UK arbitrations.



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# 10 Arbitrators' duties of disclosure in the spotlight

We expect that the Red, Orange and Green lists in the *International Bar Association Guidelines on Conflicts of Interest in International Arbitration* will continue to serve as a practical guide as to what is appropriate. However, the *Eiser* case will serve as a warning that those lists (which did not cover the scenario that arose in that case) cannot be seen as exhaustive and that arbitrators and parties must be pro-active in thinking about what scenarios could give rise to an appearance of bias and/or require disclosure. Arbitrators and parties should also be guided by relevant institutional rules, where applicable, which generally contain their own requirements as to what circumstances must be disclosed, often using a subjective rather than an objective test.

Despite this trend, we anticipate that successful challenges sufficient to justify an arbitrator's removal or an award's annulment will remain rare in practice. National courts and annulment committees will be keen to ensure that the heightened focus on arbitrators' duties is not abused by parties looking to secure a tactical advantage, if only by delaying the arbitral process. We expect that most courts will continue to deal with unmeritorious challenges robustly, especially in circumstances where timely disclosures have already been made.



**In our view, parties and their advisers should not be unduly concerned about potential challenges and should continue to see the selection of appropriately qualified tribunals and the finality of their awards as key benefits of arbitration. They should, however, ensure that appropriate due diligence has been undertaken, so as to avoid undisclosed circumstances coming to light and possibly derailing the arbitration down the line.**

Nigel Rawding QC, Partner

This trend does not necessarily mean that parties need to make different decisions about *who* they appoint to their tribunals – there remains a benefit to appointing experienced arbitrators with relevant sector expertise. We do not foresee a trend towards the appointment of arbitrators isolated from the wider arbitration community and uninvolved with other arbitrations, even in the same industry sector – as long as adequate and timely disclosures are made.

As observed in the Queen Mary and Freshfields Arbitration Lecture, delivered in December 2020:

'[L]imiting exposure by limiting overlap may appear attractive but is it right? Do we want arbitrators sitting in ivory towers...? Institutionalising the role of arbitrators risks doing damage to the very system we are trying to protect, with flexible procedures, experienced decision-makers (including with sector expertise) and selected on an inclusive basis.'

Jackie van Haersolte-van Hof, Director General of the LCIA



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# 11

## Arbitration and climate change

What role does arbitration play in the context of environmental, social and governance (ESG) issues, in particular climate change?



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## What role does arbitration play in the context of environmental, social and governance (ESG) issues, in particular climate change?

Pressure is mounting on both the public and private sectors to engage more actively in combating climate change. The arbitration community is becoming increasingly involved as disputes inevitably arise.

## Arbitration as a tool to resolve climate change-related disputes

Arbitration clauses are included in many contracts arising in the sectors that are most directly implicated by climate change, such as the energy, extractives and construction sectors. These industries, which are already heavily regulated, will likely see a further increase in regulation designed to address climate change.

According to a well-regarded research institution, there are already over 1,500 climate change-related laws and policies worldwide. This figure will inevitably grow as governments strive, in tandem with the private sector, to reach the targets set by the 2015 Paris Agreement. Disputes may arise pursuant to those regulations and/or from contracts relating specifically to energy transition.

Arbitration provides a particularly appropriate forum in which to resolve climate change-related disputes, as acknowledged by the ICC Task Force on the Arbitration of Climate Change Related Disputes – notably by giving the parties flexibility in choosing tribunals with adequate

knowledge of the relevant issues. Moreover, the arbitration process can be readily tailored to address claims by multiple parties and to accommodate *amicus curiae* interventions, which are likely to be a feature of future climate change-related arbitrations, as improvements in attribution science assist would-be claimants to overcome the causation hurdles we have typically seen in climate change-related litigation to date.

Meanwhile, the Hague Rules on Business and Human Rights Arbitration provide a tailored process for the resolution of disputes by arbitration in the context of the human rights impact of business activities – which extends to environmental and climate change-related issues. The Hague Rules draw upon the PCA's Optional Rules for Arbitration of Disputes Relating to the Environment and/or Natural Resources, which provide a bespoke procedure for environmental disputes and are already referenced in contracts such as Model Emissions Reduction Purchase Agreements.



**The climate change treaty regime establishes a range of State commitments as a matter of public international law (albeit with varying levels of enforceability). But there presently appears to be a material disconnect as between aspiration at an international level and legislation at a national level. One key challenge would appear to be providing private companies with sufficiently clear direction and regulation, at a domestic level, regarding how best to operate in such manner as to contribute meaningfully towards the goals of the Paris Agreement. Absent that, disputes will be increasingly frequent; and, more fundamentally, the common course of action required to address climate change will be lacking.**

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# 11 Arbitration and climate change

## Trade and investment treaties as a potential tool to promote sustainable development

In 2019, we noted that investment arbitration will likely play a role in determining how the economic risks associated with energy transition will be allocated. The well-reported investor-State arbitrations relating to the phase out of coal-fired power plants in various countries, and the consequent disputes over resulting compensation, are examples of this. Further, recent developments indicate that States believe investment treaties could become an effective tool actively to encourage energy transition and to help combat climate change.

The starting point for this shift is the inclusion in new or renegotiated trade and investment treaties of provisions relating specifically to climate change and sustainable development. One recent example is the EU–UK Trade and Cooperation Agreement, which regulates the economic relationship between the EU and the UK following Brexit. It requires the parties to respect the Paris Agreement, to refrain from acts or omissions that would materially defeat its object and purpose, and to encourage other countries to reduce their greenhouse gas emissions.

The proposal by the European Commission (EC) for the modernisation of the Energy Charter Treaty (ECT) is also substantially motivated by climate change-related concerns. In May 2020, the EC published a proposed revised text of the ECT, which seeks to rebalance investment protection and sustainable development objectives. The proposal further demonstrates the general shift in focus of many ‘new-generation’ trade and investment treaties from purely economic development to sustainable development.

Other related developments in the field of investment arbitration include an increased focus on mechanisms that may encourage responsible investor conduct, such as counterclaims by States for alleged breaches by investors of environmental duties and the possibility of findings of investors’ contributory fault. While the relevant case law remains relatively limited for now, there are signs that the traditional ‘one-way street’ concept of investment protection may be giving way to a more holistic approach, which recognises that foreign investment entails not only investor rights but also a measure of investor responsibility – including to the environment.



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## 11 Arbitration and climate change

### What is the arbitration community itself doing to help?

Over the past few years, the arbitration community has demonstrated its ability to facilitate change on ESG issues. In 2021, we expect to see an increased focus on better managing the significant environmental impact of arbitration, including as regards climate change.

With its win of the GAR Award for Best Development in 2020, the Campaign for Greener Arbitration (CGA) is gaining momentum. In early 2021, it will launch practical guidelines to assist arbitration stakeholders to reduce their carbon footprint. In parallel, hundreds of arbitration practitioners, arbitral institutions and law firms (including Freshfields) have signed the CGA's Green Pledge, showing their commitment to the environment, particularly around carbon reduction.

The COVID-19 pandemic has already accelerated positive behavioural change, compelling the arbitration community to rapidly embrace electronic filings and hearing bundles, as well as virtual hearings. This transformation has also demonstrated how flexible and cost-effective arbitration as a dispute resolution process can be. This trend will likely continue given inevitable corporate pressures to reduce costs in the wake of the pandemic.

A recent survey shows that

**20,000**  
trees



**or the entire tree population  
of Central Park in New York**

would be required to offset the total carbon emissions resulting from an average medium-scale arbitration.



**Our clients have moved their sustainability agendas into their core working practices and I am proud that Freshfields is able to do the same with its commitment to the Green Pledge. How we deliver our services has a profound impact on our environmental footprint and by working smarter around paper consumption, travel and other practices, we can materially reduce carbon emissions and contribute to the fight against climate change.**

Tim Wilkins, Global Partner for Client Sustainability



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